SUPPLEMENTAL SURREBUTTAL TESTIMONY OF DAVID H. GEBHARDT, JR.

Ameritech Exhibit No. 1.5

Dockets 98-0252/98-0335/00-0764 (Consolidated)

February 5, 2001

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Supplemental Surrebuttal Testimony of David H. Gebhardt, Jr.

Q. Please state your name and business address.

A. David H. Gebhardt, 1017 E. Hawthorne Blvd., Wheaton, Illinois 60187.

Q. Are you the same David H. Gebhardt who sponsored Ameritech Illinois Exhibits 1.0, 1.1, 1.2, 1.3 and 1.4 in this proceeding?

A. Yes, I am.

PURPOSE OF TESTIMONY

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to address revenue requirements-related issues and certain rate design/service cost issues raised by the Commission Staff and GCI.

RATE DESIGN/SERVICE COST ISSUES

Q. Mr. Dunkel has provided a further update to the FCC's penetration figures, based on the FCC report released in December. (GCI Ex. 9.0, pp. 2-3). Please comment.

A. Based on the FCC's December report, subscribership does appear to be more in line with prior levels. However, the fact remains that there is no negative causal relationship between Ameritech Illinois' Alternative Regulation Plan and subscribership levels in Illinois. Over the term of the Plan, Ameritech Illinois' basic local service rates remained constant or declined.

Q. Mr. Dunkel contends that targeted assistance programs are not sufficient to address the "penetration problems" in Illinois, because many customers who would qualify for them have not, in fact, requested such assistance. (GCI Ex. 9.0, pp. 5-6). Is solving the "penetration problem" an appropriate objective of this proceeding?

A. No. I do not believe that anyone –- including Mr. Dunkel –- knows why subscribership in Illinois appears low in the FCC

reports. Because its local exchange rates are generally low compared to those of incumbent LECs in other states as well as in Illinois, it is highly unlikely that Ameritech Illinois' rate levels are a root cause.

A study has been commissioned by Ameritech Illinois, the ITA and UTAC with the involvement of Commission Staff, to determine what is causing these results. This study should be available in the relatively near future. Until this analysis has been completed and reviewed, the Commission should not be trying to "solve" the problem and certainly not by reducing Ameritech Illinois' rates. If the Commission ultimately concludes that there is a subscribership issue in Illinois, it should establish a separate proceeding to determine what the problem is and evaluate the possible solutions.

Finally, Mr. Dunkel's use of FCC data from the 1983-2000 period (GCI Ex. 9.1) is irrelevant to this proceeding, which assesses the Plan over the 1995-1999 time frame. Data prior to 1995 cannot be correlated in any way with the operation of the Plan.

Q. Should the Commission's rate design decisions be driven by the fact that many customers eligible for need-based assistance plans do not take advantage of them?

A. No. There are undoubtedly many reasons why customers may choose not to take advantage of such plans. If customers conclude, for whatever reason, that they do not wish to participate in these programs, it is not the Commission's responsibility to compensate for those decisions by either rejecting rate increases which are needed, or even worse, lowering rates for all customers, the vast majority of which do not need any assistance whatsoever.

Q. Mr. Dunkel takes issue with your statement that he "distributes [access line costs] to all of the other services Ameritech Illinois provides". (GCI Ex. 9.0, pp. 17-18). Please comment.

A. Based on Mr. Dunkel's rebuttal testimony, apparently I misunderstood his proposal. In my experience, the argument that network access lines should be treated as a "shared" cost of other products and services offered by a LEC has typically resulted in an allocation, either implicitly or explicitly, of those costs to other products and services for

cost recovery purposes. In my data request response to Mr. Dunkel from which he cites only one sentence, I indicated that such an allocation was implicit in his argument that residence access line rates could be reduced even further if the Commission adopted his shared cost argument.

However, according to Mr. Dunkel, he is not proposing any such allocation. Instead, as I understand it now, the costs associated with network access lines would be excluded altogether from service cost studies and would be recovered in the contribution produced by Ameritech Illinois' overall rate structure (i.e., in the overall margins between LRSIC and rates), just as "common costs" are today.

So that there is no confusion, I do understand that Mr. Dunkel's proposal to reduce network access lines by $1.30 is not based on his shared cost theory. His shared cost theory only comes into play if the Commission chooses to reduce network access lines by an even greater amount. However, he has raised this issue in his testimony and has devoted considerable argument to it. Therefore, it is important for the Commission to understand its implications.

As I now understand Mr. Dunkel's proposal, it is far worse than I originally thought and, potentially, is destructive of rational ratemaking. Under his approach, hundreds of millions of dollars of loop costs would be eliminated from the Company's service cost studies, and would be sent into the regulatory "ether", to be recovered somehow, some way, from some customers, not otherwise identified, in overall contribution.

However, loop costs are the single largest element in Ameritech Illinois' cost structure. It is absolutely irresponsible to simply make them "disappear", without any concrete proposal as to how they should be recovered. These are facilities which Ameritech Illinois uses directly to provide core telecommunications services to its customers. Ameritech Illinois' costs associated with these lines are causally related to changes in customer demand -- one of the key determinants of what should be considered an "incremental cost". They are not like shareholder relations or corporate accounting costs which are not causally related to the demand for any product or service, and which should appropriately be recovered in overall contribution (i.e., they are truly "common costs"). It is a perversion of any economic standard

I am familiar with to treat access line costs like common costs.

It is particularly irrational to treat network access lines costs as common costs in a measured service environment like Illinois. Taken to its logical end, Mr. Dunkel's view would result in a LRSIC cost for network access lines of "0". If there is no cost basis for this rate element, how would one set a rate at all? Even in jurisdictions with flat rate service (i.e., where the access line and local usage are purchased together for a fixed price), network access line costs are routinely assigned to that package of services, along with usage costs.

By eliminating access line costs altogether, Mr. Dunkel has rendered service costs virtually superfluous in the rate design process. Without network access lines, LRSIC costs for local exchange service are so low that they provide almost no guidance relative to appropriate rate levels or rate structures. Moreover, the costs associated with performing service cost studies are considerable and, as is apparent from this proceeding, debating them in regulatory proceedings consumes considerable resources. From a cost/benefit perspective, if Mr. Dunkel's proposal is

adopted, the Commission might as well abandon cost-based pricing altogether for local exchange service and revert back to more mystical approaches, such as value of service pricing.

Q. Mr. Dunkel claims that your calculation of an embedded cost per loop did not rebut anyone's testimony. (GCI Ex. 9.0, pp. 85-86). Do you agree?

A. No. I prepared this calculation in direct response to Mr. Dunkel's testimony which claims that the cost of an access line is even lower than the LRSIC costs presented by Mr. Palmer and Staff's concerns about certain aspects of the LFAM model. I would also note that this calculation further supports the validity of my calculation of noncompetitive service earnings. The fact that network access lines constitute a large component of noncompetitive service revenues and that the embedded cost of those loops substantially exceeds their price further substantiates the fact that noncompetitive service earnings are, in fact, low.

My point -– as I made clear in my Rebuttal testimony –- was not to present a different service cost study on which rates should be based. My purpose was to provide a broader

perspective from which to view the service cost and rate design criticisms presented by Staff and GCI, as well as my noncompetitive service earnings analysis.

Q. Mr. Dunkel contends that your data request response did not provide source references which would allow him to verify your calculations. Please comment.

A. My calculations were based on ARMIS data, with which GCI is very familiar. If Mr. Dunkel could not relate my workpaper back to its ARMIS sources, I would have been happy to provide GCI with a follow-up response. They did not ask for one. I would note that both GCI generally and Mr. Dunkel in particular have insisted on follow-up responses in the past where they found the Company’s response to be inadequate. Attached as my Schedule 1 is the data request response Mr. Dunkel refers to with appropriate AMRIS source references. [I presume this is coming from Deignan.]

Q. Mr. Dunkel also expresses uncertainty about whether the accounting data you used was “intrastate” only. Please comment.

A. I cannot understand his uncertainty. Ameritech Illinois always determines the cost of a network access line on an unseparated LRSIC basis. It did so in this proceeding, as Mr. Dunkel is well aware, and has done so in every Commission proceeding involving network access line costs dating back to the early 1980's. In fact, I have provided a calculation of the embedded cost of an access line in many of these same proceedings. For consistency, I have always made this calculation on an unseparated basis as well. It would make no sense to compare the unseparated LRSIC cost of an access line to the separated embedded cost of an access line.

FAS 71

Q. In support of her proposal to eliminate the FAS 71 amortization from the 1999 level of depreciation and amortization expense, Ms. Marshall asserts that the "Commission found in Docket 92-0448 that no amortization of a depreciation reserve deficiency was appropriate for inclusion in an alternative regulatory plan" and that " the Company's "analog switching account should be amortized over a five year period which has expired." (Staff Ex. 18.0, p. 13). Does the Commission's order in Docket 92-0448/93-0239 support Ms. Marshall's position?

A. No. As I have previously discussed, the amortization of the depreciation reserve deficiency resulting from the discontinuance of FAS 71 is fully supported by the Commission's decision in Docket 92-0448/93-0239 to accept the "Company's offer to assume full responsibility for its capital recovery with no change in existing rates beyond what will be permitted beyond the price index (which will not reflect changes in depreciation expense)". The Commission found this approach to be "advantageous to rate payers and provides a reasonable solution to the capital recovery problem". (Order, p. 55.) In the later portion of the Order referred to by Ms. Marshall, the Commission concluded that an amortization of the depreciation reserve deficiency calculated by the Company in Docket 92-0448/93-0239 should not be included in the revenue requirement adopted for purposes of establishing the "going-in" rate levels under the Alternative Regulation Plan. The Commission also ruled that the analog switching account should be amortized over 5 years for the same purpose. The Commission's conclusions in this regard came in Section VI of the Order, the introduction to which states as follows:

> In a prior section of this Order the Commission found that it will no longer set depreciation rates for Illinois Bell under its alternative regulation plan and that it will allow Illinois Bell to set its own depreciation rates pursuant to generally accepted accounting principles. In this Section of the Order the Commission again addresses the depreciation issue, but only to determine the reasonableness of the going-in levels under the plan." (Order, p. 133(emphasis added)).

Thus, the decisions to reject amortization of the reserve deficiency and to amortize analog switching costs over five years went only to the "reasonableness of the going-in [rate] level under the plan" and, therefore, do not provide a basis for Ms. Marshall's proposal to eliminate the FAS 71 amortization in this proceeding.

Q. Ms. Marshall asserts that the Company's "recasting of this depreciation issue as a FAS 71 adjustment is nothing more than a second attempt to recover costs previously disallowed for rate making purposes." Does this assertion make sense?

A. No. Since the issuance of the Order in Docket 92-0448/93-0239, the overall level of non-competitive rates adopted in that case have decreased in accordance with a price cap formula which is not tied to the Company's own costs and, in particular, contains no factor related to depreciation

expense. Consistent with the conditions upon which the Commission granted the Company depreciation freedom, the Company has never sought, and does not now seek, to change either its rates, or the price cap formula, to reflect recovery of increased depreciation and amortization expenses over the level included in the "going-in" level of rates approved in Docket 92-0448/93-0239.

The issue arises in this case only because of the adjustments proposed by Staff and GCI to eliminate the FAS 71 amortization from the Company's 1999 income statement for purposes of establishing a "revenue requirement" in the event the Commission deems it appropriate to "reinitialize" rates. For the reasons I have previously discussed, a decision to "reinitialize" rates on that basis would, among other problems, have the effect of depriving the Company of the depreciation freedom granted in Docket 92-0448/93-0239.

Q. Ms. Marshall alleges that the Company's "adoption of an 8 year amortization period is simply an artificial device to assure consideration of this issue in the planned five year review of the alternative regulatory plan". (Staff Ex. 18.0, p. 14). Is Ms. Marshall's allegation valid?

A. No. Ms. Marshall offers no support for her allegation. The Company's selection of an eight year amortization period was supported by studies comparing trade-in values of electronic and digitally based consumer and professional products, computers and automobiles and light trucks with original prices. Those studies show that assets lose all service value (less salvage) over a period of 8 to 8.5 years. Similar situations have occurred with other items that have been amortized. Coincident with the establishment of Part 32 of the FCC's rules effective in 1988, compensated absences were amortized over a ten year period ending in 1997 on the regulatory books. Similarly, incurred expenses related to providing equal access to all carriers that have been deferred were amortized over an eight year period.

Q. Mr. Dunkel argues that the "FCC has specifically ordered that the telephone companies cannot amortize FAS 71 for regulatory purposes". (GCI Ex. 8.0, pp. 45-46). Does Mr. Dunkel's argument support the elimination of the FAS 71 amortization at issue in this case?

A. No. As Mr. Dunkel recognizes, the Company does not amortize FAS 71 in the interstate jurisdiction. Furthermore, as Mr. Dunkel also recognizes, the FCC does permit amortization of

FAS 71 on certain conditions. In this regard, Mr. Dunkel quotes a statement from the December 30, 1999 FCC 99-397 Order that carriers "would forego the opportunity to recover any portion of the adjustment that results from conforming their regulatory net book costs to their financial net book costs (i.e., through a below-the-line write-off)". The very next sentence from the FCC's Order, which Mr. Dunkel omits from his quote, clarifies this precondition: "As a precondition to obtaining a waiver of the depreciation prescription process, a carrier would have to voluntarily forego its opportunity to recover any portion of the one-time adjustment to regulatory books through a low-end adjustment [i.e., a one-time adjustment to increase rates to obtain a minimum prescribed return], an exogenous adjustment [to the price cap], or an above-cap filing [i.e., the establishment of higher rates than would normally be permitted under price caps]." Likewise, the Commission granted the Company depreciation freedom, including the freedom to amortize its depreciation reserve deficiency, on the condition that any change in depreciation and amortization expense will not affect the price cap formula used to set rates. The Company has strictly adhered to this condition.

Q. Ms. Marshall argues that the Commission should treat the FAS 71 write-down as a one-time event and eliminate it from rate base. (Staff Ex. 29.0, p. 3). Is Ms. Marshall's argument consistent with the position that Staff took in its direct and rebuttal presentations?

A. No. Staff has been consistent in its proposal to eliminate the FAS 71 amortization from expenses in the income statement presentations made by Mr. Voss. Staff, however, has changed its position regarding the need for a corresponding rate base adjustment. In his direct and rebuttal testimony, Mr. Voss restored the written-down assets to Ameritech Illinois' rate base, as if the write-down had not taken place, to reflect more conventional regulatory accounting. In her direct and rebuttal testimony, Ms. Marshall discussed an alternative approach (not reflected in Mr. Voss' exhibits), under which the write-down would be treated as a one-time event and eliminated from rate base. In her surrebuttal testimony, Ms. Marshall states that she has re-evaluated her position and indicates that what was her "alternative" proposal should be the approach adopted by the Commission in this case. Based on Ms. Marshall's new position, Mr. Voss has eliminated the $539.530 million restored from rate base.

Q. Is Ms. Marshall's approach to the FAS 71 adjustment reasonable?

A. No. Ms. Marshall's position is internally inconsistent. As previously discussed, her principal criticism of the FAS 71 amortization is that it is a "second attempt to recover costs previously disallowed for rate making purposes" because the Commission did not allow amortization of the reserve deficiency in 1994. If that is Ms. Marshall's theory, then the only appropriate treatment of depreciation expense in this proceeding is to calculate it on a basis that is consistent with the Commission's 1994 Order. That is, the rate base must be restated as if the write-down did not take place. That is what Mr. Voss did in his direct and rebuttal testimony. Ms. Marshall's proposal to treat the FAS 71 adjustment as a one-time event occurring outside of the test year is completely inconsistent with that theory. If the Company was not "allowed" to treat this shortfall as a reserve deficiency for ratemaking purposes in 1994, then the flip side is that the Commission should not now be "allowed" to recognize the write-down for ratemaking purposes now.

In effect, Ms. Marshall wants to have it both ways. She -- and the Commission -- did not want ratepayers to have to pay

for any reserve deficiency through rates in 1994. Now, when the Company has voluntarily written down its assets to reflect the shortfall the Commission did not want to recognize, she wants to flow through to ratepayers the entire beneficial effect of that write-down for ratemaking purposes. Such a one-sided, opportunistic approach to depreciation policy should not be adopted.

I would further note that Ms. Marshall's proposal would be unlawful under rate-of-return regulation. The Commission is legally obligated to allow regulated companies to recover their investments in regulated plant assets through depreciation expense that is reflected in customer rates. The Commission could not have required Ameritech Illinois to write down its assets in 1994. If the Commission is going to conduct an earnings analysis now based on rate-of-return principles, it cannot assume a write-down that would never have taken place. Ms. Marshall is picking and choosing regulatory constructs in a manner that is arbitrary and unreasonable.

Q. In her Surrebuttal testimony, Ms. Marshall argues that Staff's new position regarding the write-down is supported by

the Orders in Docket 92-0448/93-0239 and 96-0486. (Staff Ex. 29.0, p. 3). Is Ms Marshall correct?

A. No. Once again, Ms. Marshall erroneously relies on the Commission's decision in Docket 92-0448/93-0239 to disallow the amortization of the reserve deficiency at issue in that case for purposes of establishing the "going-in" rate level. As previously discussed, that decision does not justify Staff's position regarding amortization of the asset write-down resulting from discontinuance of FAS 71, which was undertaken in accordance with the depreciation freedom granted the Company under the Plan. Likewise, the Order in Docket 96-0486, which dealt with the Company's TELRIC cost studies and rates for interconnection, network elements, transport and termination of traffic, has nothing to do with the issues in this case. In the language from that order quoted by Ms. Marshall, the Commission referred to its decision in Docket 92-0448/93-0239 not to incorporate an adjustment for recovery of a depreciation reserve deficiency into the price cap formula. In this case, the Company is not proposing to incorporate such an adjustment into the price cap formula.

Q. Ms. Marshall and Mr. Dunkel argue that Staff's proposal to treat the write-down as a one-time event and eliminate it from rate base is consistent with the FCC's ordered treatment in the interstate jurisdiction. (Staff Ex. 29.0, p. 3; GCI Ex. 9.0, p. 46). Do you agree?

A. No. As discussed above, the condition that the FCC adopted with respect to changes in depreciation expense and customer rates is the same that the Commission adopted as part of the Plan, i.e., increases in depreciation expense resulting from the exercise of depreciation freedom are not to be recovered through increases in customer rates. There is nothing in the FCC's order which would support the "have your cake and eat it too" approach being taken by GCI and Staff, which is to (i) reflect in rate base the result of the Company having exercised its depreciation freedom, by reflecting the full effect of the FAS 71 write-down, while simultaneously (ii) removing the amortization of the write-down from expenses, thereby effectively pretending that the Company had not been granted the freedom to amortize the write-down over eight years.

GCI'S DEPRECIATION EXPENSE PROPOSALS

Q. Do you have any comments regarding GCI witness Dunkel's position regarding depreciation and amortization expense as set forth in his rebuttal testimony?

A. Yes. Mr. Dunkel proposes an adjustment to reduce the level of depreciation and amortization expense reflected in Ameritech Illinois Exhibit 7.1, Schedule 1, by $284.2 million. In support of his proposal, Mr. Dunkel, like Staff witness Marshall, proposes to eliminate the FAS 71 amortization amounts. In addition, Mr. Dunkel, unlike Staff, calculates depreciation expense using FCC depreciation rates last prescribed in 1995. Mr. Dunkel also proposes the elimination of certain other amortizations, which the Company implemented pursuant to its depreciation freedom. For all the reasons that I discussed in my Rebuttal testimony, Mr. Dunkel's "business-as-usual" regulatory approach to the calculation of depreciation expense completely negates the depreciation freedom granted by the Commission in the Alternative Regulation Order, and should be rejected.

Q. Mr. Dunkel asserts that he is “not challenging Ameritech’s freedom to ‘book’ depreciation expense starting in 1995,” but rather is “proposing that a reasonable depreciation expense should be used in the adjusted ‘test year’ data to be used to reinitialize the rates to be adopted in a revised regulatory plan”. (GCI Ex. 8.0, PP. 31-32). Do you have any response to Mr. Dunkel’s testimony in this regard?

A. Yes. Mr. Dunkel’s assertion that he is not challenging the Company’s exercise of its depreciation freedom is disingenuous. Mr. Dunkel asserts that an analysis of the data during the test year must be made to determine whether it is “reasonable” and “representative” of what is expected when the rates that result from utilizing that test year will be in effect. Mr. Dunkel, however, has presented no argument to suggest that the depreciation and amortization expense reflected in the Company’s 1999 operating income statement shown in Exhibit 7.1, Schedule 1 is not “representative”. To the contrary, his position is that the Company’s 1999 level of depreciation expense is unreasonable to the extent that it exceeds the amount of depreciation expense that would be calculated on the basis of an analysis that would be uniquely required by regulators to support depreciation rates (e.g., development of projection lives, survivor curves, historical

analysis of retirements and so forth) which were the subject of endless regulatory scrutiny in the past. As I discussed in my Rebuttal testimony, however, the intent of the Commission's 1994 decision was to free the Company from precisely this kind of second-guessing and micromanaging of capital recovery. Thus, despite his protestations to the contrary, it is abundantly clear that Mr. Dunkel is challenging the Company's exercise of its depreciation freedom. By reducing rates to reflect his adjustments to depreciation expense, the Commission would effectively be depriving the Company of its ability to manage capital recovery within the constraints of the price index –- which was one of the core objectives of the Commission's Order in Docket 92-0448/93-0239.

Q. Mr. Dunkel quotes language from the Order in Docket 92-0448/93-0239, in which the Commission stated that "any abuse [in the formulation and application of depreciation rates] will result in a reevaluation of the alternative regulatory plan pursuant to Section 13-506.1(e) of the Act". (GCI Ex. 9.0 p. 33). Has Mr. Dunkel presented any evidence that the Company has "abused" its depreciation freedom?

A. No. For the reasons discussed above and in my Rebuttal testimony, the Company's adoption of capital recovery policies which result in depreciation expense levels different from those which would result from the application of depreciation rates determined on the basis of depreciation studies traditionally required for regulatory purposes is the very essence of depreciation freedom and cannot logically be deemed to be an "abuse" of that freedom. As I discussed in my Rebuttal testimony, Ameritech Illinois would be guilty of abusing its depreciation freedom only if it had violated GAAP principles or otherwise deliberately manipulated its depreciation practice. Mr. Dunkel has presented no evidence of such an abuse. Furthermore, as shown on GCI Exhibit 9.9, most of Mr. Dunkel's proposed adjustments to depreciation expense is attributable not to the use of different depreciation rates, but to his proposal to eliminate the FAS 71 amortization and certain other reserve deficiency amortizations. Mr. Dunkel has not alleged, nor is there any evidence to support any allegation, that these amortizations constitute an "abuse" of the Company's capital recovery freedom. In this regard, GCI was asked in data requests whether it is Mr. Dunkel's opinion that the Company's decisions to (i) amortize the FAS 71 write-down over eight years and (ii) to amortize the reserve deficiencies discussed

at pages 49 to 50 of his rebuttal testimony, were “abuses” of the depreciation freedom granted in Docket 92-0448/93-0239. (Ameritech Illinois’ Sixth Set of Data Requests to GCI, Items 13 and 16.). (GCI Ex. 9.0, pp. 49-50). Although GCI’s responses to those requests reiterate Mr. Dunkel’s position that the referenced amortizations should not be included in the 1999 adjusted “test year” data, the responses studiously avoid a direct answer to the question of whether those amortizations reflect an “abuse” of the Company’s depreciation freedom.

Q. Mr. Dunkel suggests that you have testified that the Company was granted freedom not to follow the Joint Board (Part 36) jurisdictional separations requirements for depreciation expense and reserves. (GCI Ex. 9.0, pp. 33-34). Did Mr. Dunkel accurately characterize you testimony?

A. No. I have never stated that the Company is no longer required to follow the FCC’s Part 36 jurisdictional separations rules. Moreover, as discussed by Mr. Dominak, the Company does comply with those rules. What I did state was that, pursuant to its depreciation freedom, the Company does not rely on the FCC’s historical conventions such as

projection life, curve shape, and other parameters in setting its depreciation rates.

Q. Mr. Dunkel argues that Ameritech Illinois made a “significant admission” in the portion of your Rebuttal testimony where you showed that depreciation expense would be $388 million using FCC approved parameters and $354.3 million using ICC approved parameters, compared to Ameritech Illinois’ 1999 depreciation expense of $666.5 million. (GCI Ex. 9.0, pp. 30-31). Do you have any comments in response to Mr. Dunkel’s argument?

A. Yes. I do not believe that my testimony on this point can be fairly characterized as an “admission”. In this regard, it should be noted that the depreciation amounts calculated based on the FCC and ICC parameters do not reflect an amount for FAS 71 amortization. The Company has never claimed that the use of ICC or FCC parameters, with no inclusion of FAS 71 amortization, would not result in a lower depreciation expense amount. Rather, the Company has maintained that an adjustment to reduce the amount of depreciation expense to the amount that would be calculated based on application of such parameters would be improper for all the reasons I have discussed.

Q. Mr. Dunkel accuses you of presenting data in your rebuttal testimony that "misrepresents the depreciation expense that the Company is claiming in this proceeding." (GCI Ex. 9.0, p. 51). Is this a fair accusation?

A. No. Mr. Dunkel is referring to page 105 of my Rebuttal testimony where I presented a comparison of the Company's composite depreciation rate and depreciation expense excluding the FAS 71 amortization, with the composite depreciation rates and depreciation expense for the FCC approved parameters, ICC approved parameters, and the low end of the FCC's range of service lives. Mr. Dunkel argues that I "misrepresented" the Company's claimed level of depreciation expense by deducting $110 million of amortization from the amount shown while not making a similar deduction from the FCC and ICC parameter figures.

There was, however, no "misrepresentation". To the contrary, my testimony makes quite clear that I subtracted the amortization expense from the Company depreciation figure and explains why I did so. I provided the referenced comparison in response to Mr. Dunkel's direct testimony in which he argued that the Company's depreciation rates are unreasonable

based on a comparison of the Company's composite depreciation rate to rates developed using the FCC and ICC parameters. As I discussed, the problem with Mr. Dunkel's analysis was that he had developed Ameritech Illinois' composite rate including FAS 71 amortization, whereas the composite rate and depreciation expense calculated on the basis of the ICC and FCC parameters do not reflect FAS 71 amortizations. Accordingly, I presented an apples-to-apples comparison by excluding the effect of the FAS 71 from the calculation of the Company's composite depreciation rate. This was an appropriate presentation for purposes of rebutting Mr. Dunkel's assertions that the depreciation rates being used by the Company are unreasonable in comparison to rates developed on the basis of the FCC and ICC parameters.

Q. Mr. Dunkel dismisses the comparison of Ameritech Illinois' accrual ratio with competitor companies, saying that the FCC has not found such comparisons appropriate due to the differences in equipment used by those companies. (GCI Ex. 9.0, p. 59). How do you answer Mr. Dunkel?

A. I respond to Mr. Dunkel the same way I would respond to the FCC, if asked. The plain facts are that these companies are in similar businesses, they use switching and cabling from

the same manufacturers, and Ameritech Illinois' accrual rates –- no matter how Mr. Dunkel calculates them -– are below those of the comparator group. It is just not realistic to ignore such information and blindly lower accrual rates so that the difference is even greater than it is.

Q. Mr. Dunkel maintains that the Company had a reserve surplus at the beginning of 1999. (GCI Ex. 9.0, p. 50). Is Mr. Dunkel's analysis correct?

A. No. Mr. Dunkel's assertion that there is a reserve "surplus" is based entirely on a calculation of a theoretical reserve using a formula which incorporates the same FCC depreciation lives which Mr. Dunkel claims should be used to calculate depreciation expense. Thus, Mr. Dunkel's argument is circular: he uses a calculation of a theoretical reserve "surplus" using his proposed service lives to support an argument that there is no reserve deficiency and, therefore, the Commission should adopt Mr. Dunkel's proposed service lives. Because the Company does not rely (and is not required to rely) on the FCC's service lives and methods for purposes of setting intrastate depreciation rates, Mr. Dunkel's construct is of no value.

Q. In his Rebuttal testimony, Mr. Dominak testified that if the Commission were to adopt Mr. Dunkel's proposal with respect to depreciation expense, it would be necessary to adjust the accumulated depreciation reserve to reflect the amounts that would have been accrued on the basis of Mr. Dunkel's proposed depreciation rates since 1994. Mr. Dunkel takes issue with Mr. Dominak's testimony in this regard, stating that "GCI adjusted the depreciation reserve in the same way Mr. Dominak did". (GCI Ex. 9.0, p. 33) Do you have any comments in response to Mr. Dunkel's testimony on this point?

A. Yes. Mr. Dunkel claims that "[b]oth Mr. Dominak and Mr. Smith reduced the depreciation reserve by the same amount as they reduced the depreciation expense". The nature of the depreciation expense adjustments made by Mr. Dominak and Mr. Smith were, however, significantly different from one another. Mr. Dominak made an adjustment to reduce 1999 depreciation expense by the amount of depreciation inadvertently recorded for accounts that had already been fully depreciated at the beginning of 1999. Consistent with that adjustment, an adjustment was made to remove from the depreciation reserve the amount of the depreciation expense that had been improperly booked to that account. By contrast, Mr. Smith's depreciation expense adjustment

includes the impact of Mr. Dunkel's proposals to eliminate FAS 71 and to calculate depreciation expense based on FCC depreciation rates prescribed in 1995, thereby effectively negating the depreciation freedom granted by the Commission in Docket 92-0448/93-0239. For the reasons previously discussed with respect to Staff witness Marshall's position regarding FAS 71, if the Commission sets depreciation expense as if the Company had not been granted depreciation freedom in 1994, then consistency requires that the depreciation reserve be calculated on the basis of the same assumption.

DIRECTORY ISSUES

Q. Mr. Smith reduced his recommended imputation of Yellow Pages revenue to Ameritech Illinois from $163 million annually to $126 million annually. (GCI Ex. 6.2, p. 31). What was the reason for this reduction?

A. Mr. Smith reduced his proposed imputation based upon information provided by Ameritech Illinois in discovery that an imputation of $163 million would exceed Ameritech Publishing, Inc.'s ("API") gross income from directory operations in Illinois by over $11 million dollars. Mr. Smith recognized that API could not be expected, under any

circumstances, to pay Ameritech Illinois more money than API actually made.

Q. Does Mr. Smith's reduction in the amount of his proposed imputation make imputation any more reasonable?

A. No. The theory that has been used to justify imputation of Yellow Pages revenue in Illinois and elsewhere is that the public utility has acted improperly in breach of some legal obligation owed to ratepayers and as a result ratepayers have been harmed. Mr. Smith does not even attempt to identify any alleged duty that Ameritech Illinois supposedly breached that would support imputation. Rather, he bases his proposed imputation on statements made by the Commission in its order in Dockets 92-0448/93-0239, which he quotes at page 36 of his rebuttal:

> Under Section 7-102(2) of the Public Utilities Act (PUA), the Commission has jurisdiction over affiliated interests having transactions with public utilities under the Commission's jurisdiction. API is an affiliate of IBT.

The Commission has always included revenues from IBT's Yellow Pages advertising in the calculation of the Company's revenue requirements. The issue before the Commission is to

determine the appropriate amount of revenues from Yellow Pages advertising that will count against IBT's revenue requirements.

Mr. Smith concludes from these statements that the Commission has jurisdiction over API and general authority to impute to Ameritech Illinois any amount of API's advertising revenues that the Commission deems appropriate. Mr. Smith states: "Thus, the Commission can determine the appropriate amount of revenues from Yellow Pages advertising that will count against IBT's revenue requirement. . . ." (Smith Rebuttal at p. 37). Mr. Smith contends that whether or not Ameritech Illinois could ever achieve this level of payments from API in the real world is absolutely irrelevant: "Thus, the actual level of payments from API to IBT that API has been making or would 'agree' to make is not determinative of the amount of Directory Revenue that should count against IBT's intrastate revenue requirement." (Smith Rebuttal at p. 36).

Q. Is Mr. Smith's reliance upon the Commission's reference in its prior order to Section 7-102(2) of the Act appropriate?

A. No. Mr. Smith has failed to quote important parts of Section 7-102(2). What that section actually states is:

> The Commission shall have jurisdiction over affiliated interests having transactions . . . with public utilities under the jurisdiction of the Commission, to the extent of access to all accounts and records of such affiliated interests relating to such transactions. . . . (emphasis added). 220 ILCS 5/7-102(2).

Thus, Section 7-102 does not grant the Commission plenary authority over affiliated interests or empower it to impute revenues from the affiliated interest to the utility as Mr. Smith implies. Section 7-102(2) merely grants the Commission access to the affiliated interest's accounts and records to the extent necessary to permit the Commission to determine the reasonableness of transactions between the utility and the affiliated interest.

Q. Mr. Smith contends that the appellate court held that the Commission did have jurisdiction over API and the yellow pages. (GCI Ex. 6.2, p. 41). Is he misreading the appellate court's opinion?

A. Yes. The appellate court specifically stated:

> Section 7-102(c) provides the Commission with jurisdiction over transactions between public utilities and affiliated interests "to the extent of access to all accounts and records of such

> affiliated interests related to the transactions." . . . This provision protects against transactions which financially exploit public utilities to the detriment of those they serve, the ratepayers. . . . The present case, in which ratepayers would be forced to bear the burden of an increased revenue requirement caused by Bell's foregoing an opportunity to increase directory revenues, involves just such a transaction. *Illinois Bell Telephone Company v. Illinois Commerce Commission,* 283 Ill App. 3d 188, 669 N.E. 2d 919, 931(1st Dist. 1996)(emphasis supplied).

The appellate court upheld the imputation in that case because of an improper transaction that allegedly disadvantaged ratepayers (Ameritech's abrogation of Ameritech Illinois' exclusive option to renew the directory agreement). However, the appellate court did not hold that the Commission had jurisdiction over API or the yellow pages. The key difference between the last case and the present proceeding is that Mr. Smith has not even attempted to identify an allegedly improper transaction upon which to base a new imputation.

Q. Is Mr. Smith's reliance upon the Commission's second statement in its prior order reasonable?

A. No. Mr. Smith has quoted the Commission's statement out of context. Earlier in its order, the Commission recited the

history of Ameritech Illinois' involvement in the Yellow Pages:

Mr. Willenborg described the history of Yellow Pages directory publishing in Illinois Bell's service territory. Donnelley has been the exclusive publisher of Yellow Pages directories for over 70 years. As publisher, Donnelley has owned the content of and has held the copyright to the Yellow Pages directories, and owns and maintains all advertising records and customer contracts. In contrast, Illinois Bell never has owned or controlled Yellow Pages assets or the revenues that are derived from them. Rather, it always has been in the position of providing certain products and services (listing information, billing and collection, database functions, and the right to co-bind the Yellow Pages with the White Pages) to Donnelley, Am-Don or DonTech for compensation pursuant to written directory agreements approved by the Commission. Historically, and under the current Directory Agreement, only the net amounts received by Illinois Bell for services rendered and products delivered, after covering directory expenses has been taken into consideration, have been used by the Commission in determining the Company's intrastate rates. (ICC Docket No. 2-0448/93-0239, Order, October 11, 1994, p. 98).

The Commission's statement about including "revenues from IBT's Yellow Pages advertising in the calculation of the Company's revenue requirements" must be read in context with these actual facts of the directory relationship as acknowledged by the Commission. The reference to "revenues from IBT's Yellow Pages advertising" clearly was a reference to the revenues Ameritech Illinois received under the Directory Agreement for providing services to the directory publisher. That this was the intent of the Commission's statement is clear from the basis for the Commission's imputation order. The Commission did not impute advertising revenues to Ameritech Illinois based upon its assessment of what share of advertising revenues should belong to Ameritech Illinois. Rather, the Commission imputed additional revenues to Ameritech Illinois based upon its assessment of the level of payments Ameritech Illinois could have negotiated for its services under the Directory Agreement if Ameritech Illinois had exercised the bargaining power it allegedly possessed by reason of its exclusive renewal option. (ICC Docket No. 92-0448/93-0239, Order, October 11, 1994, pp. 101-103). No matter how many times Mr. Smith or other witnesses choose to quote the Commission's statement, they can not change the

underlying facts or change the actual basis for the Commission's prior order.

Q. Mr. Smith states that the appellate court affirmed the Commission's prior order. (GCI Ex. 6.2, p. 37). Does the appellate court decision support Mr. Smith's interpretation of the Commission's order?

A. No, consistent with the Commission, the appellate court held that when Ameritech Corporation guaranteed that Ameritech Illinois would renew the 1984 Directory Agreement for an additional five years from 1995-1999, Ameritech usurped Ameritech Illinois' exclusive option to renew the Agreement (in violation of Section 7-203 of the Act) without Commission approval (in violation of Section 7-102 of the Act). The Court held that there was sufficient record evidence to support the Commission's finding that the exclusive option to renew, had it not been usurped, would have given Ameritech Illinois significant bargaining power with Donnelley that it could have used to increase its payments under the Directory Agreement. Mr. Smith's quotation from the appellate court opinion confirms that this was the basis for the Court's ruling. (GCI Ex. 6.2, p. 39). Contrary to Mr. Smith's implication, the Court did not hold that the Commission had

general authority to decide what portion of API's advertising revenues should be imputed to Ameritech Illinois in the absence of any improper conduct by Ameritech Illinois and in the absence of any legitimate business reason why API should make such payments.

Q. Mr. Smith contends that you are wrong when you state that the Commission's decision about yellow pages in this proceeding must be based upon whether the contractual payments Ameritech Illinois currently is receiving from API are consistent with what Ameritech Illinois would be receiving if it had negotiated at arm's length with a non-affiliated publisher. (GCI Ex. 6.2, p. 39). What is his basis for this statement?

A. Mr. Smith's contention that the results of an arm's length transaction are irrelevant is consistent with his (incorrect) position that the Commission has plenary jurisdiction over the yellow pages and API and does not need a legal rationale for imputing yellow page revenues to Ameritech Illinois. The only actual explanation he provides for the alleged irrelevance of an arm's length transaction is that the current situation is the result of the affiliated interest transaction, which the Commission found improper in Docket 92-0448/93-0239, and which the appellate court affirmed.

This argument makes no sense since the whole basis for the Commission's 1994 imputation was that Ameritech Illinois had failed to enter into an arm's length transaction with the directory publisher.

Q. Does the Commission's decision in Docket 92-0448/93-0239 control the outcome in this case?

A. No. Each case must be decided upon its own merits based upon the facts existing at the time of decision. What the Commission determined in Docket 92-0448/93-0239 was that test year revenues in that docket would have been increased by $51 million dollars if Ameritech Illinois had bargained at arm's length with Donnelley and API to increase its payments under the 1984 Directory Agreement in exchange for exercising it unilateral right to renew the Directory Agreement for five years through the end of 1999. The Commission did not purport to decide what Ameritech Illinois' directory revenues would be for any future test year and, in particular, for periods after the renewed Directory Agreement expired on December 31, 1999.

Q. Mr. Smith contends that if APII (Ameritech Publishing of Illinois, Inc.) had made payments of $126 million (the amount

of his proposed imputation) to Ameritech Illinois in 1999, APII still would have earned 37.8% on average common equity or 44.4% on APII's year-end common equity. (GCI Ex. 6.2, p. 35). Please comment?

A. APII's return on equity is irrelevant in this context and is not a proper basis for the Commission to impute a portion of APII's earnings to Ameritech Illinois. As I stated earlier, the Commission may only impute revenues or profits to Ameritech Illinois to the extent that the Commission determines, based upon real evidence, not speculation, that but for some improper conduct by Ameritech Illinois or an affiliate to the detriment of ratepayers, Ameritech Illinois is receiving less revenues than it would have been receiving under an arm's length transaction. Such evidence has not been presented. Furthermore, I have no doubt that some or all of the independent directory publishers that purchase listings from Ameritech Illinois at $0.04 per listing also have similar or higher returns on equity; yet, Mr. Smith is not suggesting that the Commission impute revenues or profits to Ameritech Illinois from these publishers.

Q. Mr. Smith persists in his argument that the imputation issues in the state of Washington and Illinois are similar. (GCI Ex. 6.2, p. 38). Do you have any further comment?

A. My only comment is that Mr. Smith is consistent -- consistently wrong. In Washington, PNB transferred the yellow pages assets that it owned to an affiliate without obtaining reasonable compensation for the benefit of ratepayers. PNB's improper gift of its yellow page assets justified the imputation. In Illinois, there has been no asset transfer -— and thus no improper transaction -- because Ameritech Illinois never owned any yellow page assets. No amount of obfuscation can change those facts.

Q. Mr. Smith notes Ameritech Illinois' response to a data request that there is no statute or regulation that would preclude Ameritech Illinois from publishing a yellow pages and attempting to charge rates similar to what API and DonTech charge. (GCI Ex. 6.2, p. 40). What is the pertinence of this comment?

A. I have no idea. The pertinent question is not whether there is any law or regulation that precludes Ameritech Illinois from entering the yellow pages classified advertising

business, but whether there is any law or regulation that obligates it to do so. The answer is no. The Commission's regulations require Ameritech Illinois to publish (or have published) a white page alphabetical directory that is delivered annually to each of its customers. (83 Ill. Admin. Code Section 735.180). There is no similar requirement for the yellow pages.

Mr. Smith appears to be suggesting that the Commission should impute classified advertising revenues to Ameritech Illinois because it has not entered a non-regulated business that it has no legal or regulatory obligation to enter and that the Commission has no power to force it to enter. Ameritech Illinois has never published a yellow page directory, and the Commission has never had a problem with that decision. It was explicit in the 1984 Directory Agreement that Ameritech Illinois would continue in its traditional role as a provider of services to the yellow page publisher and that Ameritech would enter the directory publishing business through a separate, unregulated affiliate. The Chairman of the Commission helped to negotiate that Agreement, and the Commission approved the Agreement as being in the public interest.

Q. Do you have any comment on Mr. Smith's Schedule E-1?

A. Yes. In his Schedule E-1, Mr. Smith describes three methods by which the Commission might decide how much directory advertising revenue to impute to Ameritech Illinois. Mr. Smith's analysis assumes that the Commission has discretion to impute any amount of advertising revenues it desires to Ameritech Illinois.

However, the Commission may only impute directory advertising revenues to Ameritech Illinois' regulated accounts if it finds, based upon substantial evidence, that because of some improper conduct by the Company to the detriment of ratepayers, Ameritech Illinois is receiving less revenue from API or another publisher than it would have received in an arm's length transaction. Similarly, the amount of the imputation must bear a reasonable relationship to the value lost by ratepayers as a result of the alleged improper conduct. That is, how much additional revenue would have the Company received from API or another publisher if Ameritech Illinois had acted properly. Mr. Smith's Schedule E-1 does not even address this subject.

Q. Although Mr. Smith has not done so, does Mr. Dunkel attempt to identify any allegedly improper conduct by Ameritech Illinois that was detrimental to ratepayers?

A. Mr. Dunkel states: “If Ameritech Illinois were to contract with an unaffiliated publisher, Ameritech Illinois would be able to obtain a publishing fee (or retain a portion of the yellow pages revenues as its publishing fee). By using an affiliated publisher selected through a ‘no bid’ contract, Ameritech Illinois is losing substantial revenues which it could otherwise obtain.” (GCI Ex. 9.0, p. 27).

Q. Does Mr. Dunkel attempt to quantify the amount of additional revenue Ameritech Illinois allegedly could have received by contracting with an unaffiliated publisher?

A. No, Mr. Dunkel does not indicate whether this amount would be $10 or $10 million. He makes no attempt whatever to quantify what additional revenues Ameritech Illinois would have received from an unaffiliated publisher. Nor does any other witness.

Q. How do you respond to Mr. Dunkel’s contention that an unaffiliated publisher would make substantial payments to

Ameritech Illinois if Ameritech Illinois contracted with it instead of API?

A. I am perplexed as to why Mr. Dunkel thinks unaffiliated publishers would pay substantial “publishing fees” to Ameritech Illinois. The primary services Ameritech Illinois provides to publishers are listing services (which it is required to provide at $0.04 per listing) and billing and collection services (which most publishers do not need or want). Unaffiliated publishers do not need a directory agreement with Ameritech Illinois to obtain these services.

If an unaffiliated publisher did contract with Ameritech Illinois, one of the contract requirements would be that the publisher print and distribute to every Ameritech Illinois customer on an annual basis a white page alphabetical directory, including the standalone Chicago alphabetical directory. The publisher would be required to satisfy Ameritech Illinois’ other directory obligations under the Commission’s rules, as well. Since the publisher would incur substantial incremental expenses to satisfy these directory obligations if it contracted with Ameritech Illinois, it is more likely that the publisher would demand compensation from Ameritech Illinois than that the publisher would offer

Ameritech Illinois a substantial "publishing fee." This would seem to explain why no independent directory publisher has contacted Ameritech Illinois seeking to enter into a "publishing agreement" of the type Mr. Dunkel describes.

Q. How do you respond to Mr. Dunkel's suggestion that Ameritech Illinois should have solicited bids for the services it provides and receives from API?

A. Here again, Mr. Dunkel fails to identify what it is that Ameritech Illinois was supposed to put out for bid that publishers could be expected to bid to provide. When the circumstances that exist today are compared with the circumstances that existed in 1984, when Ameritech Illinois last entered into a Directory Agreement that provided subsidies to ratepayers, it becomes clearly apparent that Ameritech Illinois had no bargaining leverage left by 1999 that would have induced a publisher (affiliated or unaffiliated) to "bid" to pay "publishing fees" to Ameritech Illinois.

In 1984, Ameritech Illinois owned and controlled its customer listings and was under no legal obligation to provide them at a uniform price to everyone. If a directory publisher wished

to obtain listing information, it had to pay the price Ameritech Illinois established for those listings. If a publisher wanted preferential access to those listings or wanted to obtain them in a special format, it had to pay substantially more for the listings than what other publishers were charged. Ameritech Illinois' ownership of its listings gave it substantial bargaining power to negotiate above-cost payments from directory publishers and even higher payments from a preferred publisher. Today, by contrast, Section 222(e) of TA 96 prohibits Ameritech Illinois from discriminating in favor of, or against, any directory publisher with respect to directory listings, and FCC rules preclude Ameritech Illinois from charging more than $0.04 per listing for its listing information. Ameritech Illinois' current bargaining power based upon its listing information is zero.

In 1984, Ameritech Illinois did not offer billing and collection services to directory publishers at standard rates. Ameritech Illinois had significant bargaining power to negotiate above-cost payments in exchange for providing these services on an exclusive basis to a preferred publisher. Today, Ameritech Illinois offers billing and collection services at standard rates to any directory

publisher. Furthermore, most directory publishers do their own billing and collection or contract with a billing firm and are not interested in Ameritech Illinois' billing and collection services. (A change that has made Ameritech Illinois' billing and collection services less attractive to publishers is the statement on the customer's bill that telephone service will not be affected by failure to pay directory advertising charges.) Ameritech Illinois' current bargaining power based upon its billing and collection services is zero.

In 1984, Ameritech Illinois owned the copyright on the white page alphabetical directories. A directory publisher that attempted to co-bind a white page directory with its yellow pages potentially violated Ameritech Illinois' copyright, and Ameritech Illinois actively enforced its copyright. Thus, a publisher that wished to co-bind the white pages with its yellow pages had to be willing to make significant payments to Ameritech Illinois or risk a copyright infringement suit. Today, white page alphabetical directories are in the public domain, and any directory publisher can co-bind the white pages and yellow pages without any payment to, or permission from, Ameritech Illinois. (I am informed that the United States Supreme Court struck down the telephone companies'

copyright in the white pages in a case called Feist Publications v. Rural Telephone Service Company decided in 1991.) Ameritech Illinois' current bargaining power based upon co-binding the yellow pages with Ameritech Illinois' white pages is zero.

In summary, all of the reasons that traditionally caused directory publishers to make directory payments to Ameritech Illinois are gone. Ameritech Illinois did not contract with an unaffiliated publisher in exchange for a publishing fee in 1999 because Ameritech Illinois had no bargaining power to obtain such payments.

Q. If your position is correct as to Ameritech Illinois, how do you explain Mr. Dunkel's statement that "Independent publishers bid for an independent ILEC's directory business, and are willing to pay the ILEC's [sic] 'publishing fees' (or allow the ILEC to retain a portion of the directory advertising revenues as its publishing fee)?" (GCI Ex. 9.0, p. 27).

A. While Mr. Dunkel makes this statement, he does not provide a single example of an independent directory publisher that pays a "publishing fee" to an independent ILEC of the type he

describes. Ameritech Illinois submitted l data requests to GCI asking Mr. Dunkel specifically to identify those independent directory publishers that pay these publishing fees and the independent ILECs that receive these fees so that Ameritech Illinois could compare and contrast those publishing arrangements with Ameritech Illinois' situation. I attach a copy of those data requests as Schedule 2. GCI's response was to object to the requests. One such objection stated:

> GCI objects to this request as overly broad and burdensome. In addition, the directory publishing agreements that exist between ILECs and their publishers are routinely classified as proprietary. Mr. Dunkel has participated in over 130 telecommunications regulatory proceedings, and has testified before over one-half of the state utility regulatory commissions in the United States over a period in excess of 20 years. In addition, this information may be available to Ameritech as it is already well aware of over 200 independent publishers, as stated on page 11 of the rebuttal testimony of Ameritech witness Mr. Barry.

If Mr. Dunkel has testified over 130 times in over half the states for more than 20 years, surely, he ought to be able to identify several specific publishers who make these payments and several specific ILECs who receive them, as well as provide specific information on how those agreements are structured.

At another point in the data responses, GCI states that "The standard practice in the industry is that unaffiliated publishers pay ILECs a publishing fee, or allow the ILECs to retain a portion of the directory advertising revenues as their publishing fee, in return for the ILEC selecting that publisher for the ILEC endorsed directory in the ILEC's service area." Surely, if these payments are standard industry practice, Mr. Dunkel ought to be able to identify several specific publishers who make these payments and several specific ILECs who receive them, as well as provide specific information on how those agreements are structured. Yet, Mr. Dunkel provides no examples.

There are several reasons why an independent directory publisher may be making payments to an ILEC, but without knowing the exact nature of the relationship and the situation of the parties, it is impossible to know whether the situation is comparable to Ameritech Illinois' situation in Illinois. For example, independent publishers may be paying ILECs for listings or other services performed by the ILEC just as independent publishers pay Ameritech Illinois. Such situations would not affect the outcome of the current proceeding.

It may be that the ILEC was the traditional publisher of the yellow pages, and the directory publisher is buying the business from the ILEC. This was the situation in the state of Washington as I described in my rebuttal testimony, and it is totally dissimilar to the situation in Illinois.

It may be that the ILEC owns and publishes the yellow pages and pays contract fees (or allows the contractor to retain a portion of the advertising revenues) in exchange for services provided by the contractor. This appears to be the situation in Alaska with respect to the Matanuska Telephone Association, which is the only ILEC GCI identified in its data responses, and these may be the situations generally to which Mr. Dunkel was referring. However, these situations are the polar opposite of the situation in Illinois, where a non-regulated publisher controls the publishing rights and the customer relationships and pays the telephone company at market rates only for those services it needs. Thus, these situations should have no bearing on the outcome in Illinois.

In summary, without specific examples that can be compared and contrasted to Ameritech Illinois' situation in Illinois,

Mr. Dunkel's generalized comments provide no useful information.

Q. Mr. Dunkel discusses his earlier testimony regarding Ameritech Illinois' alleged endorsement of the directories by the use of the Ameritech name on the directories. GCI Ex. 9.0, p. 26). He states that he does not contend that the Illinois Bell or Ameritech Illinois names appear on the directories. Rather, he states that customers do not appreciate the distinction between "Ameritech" and "Ameritech Illinois" and associate the "Ameritech" brand name on the directory cover with Ameritech Illinois. Mr. Smith makes a similar comment. (GCI Ex. 6.2, p. 38). What is the point of these contentions?

A. The name issue is an outgrowth of Mr. Dunkel's unsubstantiated contention that unidentified independent directory publishers would be willing to pay some unspecified amount of money for the right to include the local telephone company's name or other endorsement on their directories. Mr. Dunkel contends that because independent publishers allegedly are willing to pay for Ameritech Illinois' endorsement, then API should be required to pay for the endorsement as well. However, Ameritech Illinois does not

endorse API's directories and Ameritech Illinois' name does not appear on the directories. Consequently, Mr. Dunkel's argument is stillborn. In an attempt to resuscitate the argument, Mr. Dunkel is forced to argue that API's and Ameritech Illinois' use of a common brand name in marketing their respective products constitutes an endorsement by Ameritech Illinois of API's directories for which Ameritech Illinois should be paid.

Q. How do you respond to this argument?

A. First of all, the argument is pointless because, as pointed out above, Mr. Dunkel has presented absolutely no evidence that independent directory publishers would be willing to pay money for use of the Ameritech name nor has he provided any evidence of how much they would pay.

Second, the argument is pointless because Ameritech Illinois does not own or control the use of the Ameritech brand and could not license either API or an independent publisher to use it. Ameritech Corporation created and owns the brand; if a directory publisher were willing to pay to use it, those payments would have to be made to Ameritech Corporation, not Ameritech Illinois.

Third, the argument is circular. If API should pay Ameritech Illinois for API's use of the brand, then should not Ameritech Illinois likewise pay API for Ameritech Illinois' use of the brand. After all, API has used the brand for ten years longer than Ameritech Illinois and has spent large sums to build brand equity. Ameritech Illinois has only recently begun to spend money to build the brand, and Mr. Smith and Mr. Dunkel both propose (incorrectly) to disallow those expenditures from Ameritech Illinois' revenue requirement. Moreover, if API should pay Ameritech Illinois for use of the brand, then would Mr. Dunkel contend that Ameritech Mobile, Ameritech Security Link and Americast also should pay Ameritech Illinois for their use of the brand, or, more appropriately, should not Ameritech Illinois pay these companies for its use of the brand? The point is that each of the Ameritech affiliates enjoys substantial benefits from using a common brand and each separately promotes the brand with respect to its separate products. However, that creates no right to, or rationale for, payments between the entities.

My final comment is that neither Mr. Dunkel nor Mr. Smith provides any support for his supposition that customers associate the Ameritech brand on the directories with

Ameritech Illinois, and I think they are wrong. I attach as my Schedule 3, copies of the cover and the third page of the current Glen Ellyn-Warrenville-West Chicago-Wheaton-Winfield directory. I believe that when customers see the name "Ameritech" on the cover with the copyright "© 2000 Ameritech Publishing, Inc.", they associate "Ameritech" with "Ameritech Publishing, Inc.," not Ameritech Illinois. This is especially true since the Ameritech name was used on the directories published by the Donnelley/API partnership for 10 years before Illinois Bell even began using the "Ameritech Illinois" assumed name or the Ameritech brand. Furthermore, if the customer opens the directory to the third page labeled "Telephone Provider Information," the customer sees several local telephone companies listed in alphabetical order. All the companies receive equal prominence and are listed in the identical fashion. At the bottom of the page, there is a statement, "For further information regarding telecommunication and telephone services, look in the Ameritech Yellow Pages under "Telephone Companies." Thus, the directory is specifically disassociated from any particular telephone company, including Ameritech Illinois. The directory contains no endorsement of Ameritech Illinois by API and no endorsement of API by Ameritech Illinois. In short, there is absolutely nothing in the directory that

would suggest or imply to customers that Ameritech Illinois "endorses" the directory.

Finally, the directory cover displays the SBC Global Communications logo, but it does not contain the Ameritech logo. This is yet another reason why customers would be unlikely to associate Ameritech Illinois with the directory.

Q. Mr. Smith states that even though Ameritech Illinois' non-product corporate image building advertising expenses have been and allegedly should be disallowed, Ameritech Illinois' product advertising, which includes the Ameritech name with respect to those products, has not been disallowed. (GCI Ex. 6.2, p. 37). Therefore, Ameritech Illinois' product advertising reinforces the use of the name. How do you respond?

A. Ameritech Illinois' product advertising reinforces the use of the Ameritech brand in connection with Ameritech Illinois' products. It does not reinforce the use of the brand in connection with Ameritech Publishing's products. Ameritech Publishing pays for that advertising. As I stated earlier, the fact that Ameritech Illinois obtains a benefit from advertising its products under the common Ameritech brand

does not create a reason why Ameritech Publishing should make any payments to Ameritech Illinois.

Q. Mr. Dunkel takes issue with your statement that any yellow pages revenue imputation would be used to subsidize local telephone services, and he references your response to supplemental data responses. (GCI Ex. 9.0, p. 29). Do you have any further comment on this issue?

A. Yes, what I agreed to in data responses was that when I referred to the stated purpose of yellow page imputation as being to "subsidize local telephone services," I did not necessarily mean to imply that directory revenues would be used to price local telephone services below their properly calculated LRSICs. Rather, what I meant was that the subsidy from a directory revenue imputation would be used to price local telephone services lower than they would otherwise be priced without the imputation.

However, the fact that the directory imputation might not lower local telephone rates below LRSIC does not mean that a directory imputation would not subsidize local rates. Section 13-507 of the Act recognizes that from a revenue perspective, a service's costs should include a reasonable

portion of common and overhead costs and requires that the Commission "establish rates or charges for the noncompetitive services which reflect only that portion of the facilities or expenses that it finds to be properly and reasonably apportioned to noncompetitive services." (220 ILCS 5/13-507). If the Commission were to impute non-regulated advertising revenues to Ameritech Illinois' regulated accounts and use that imputation to offset common and overhead costs reasonably apportioned to noncompetitive services, then the Commission would violate the spirit of Section 13-507.

Similarly, a directory imputation that would allow local exchange services to be priced at artificially low levels would violate the spirit of Section 263(a) of TA 96. This section provides:

> No State or local statute or regulation, or other State or local legal requirement, may prohibit or have the effect of prohibiting the ability of any entity to provide any interstate or intrastate telecommunications service.

Inevitably, a fictitious yellow page subsidy of local exchange services that resulted in lower local exchange

service rates would make it harder for other providers to compete for these services.

CONCLUSION

Q. Does this conclude your Surrebuttal testimony?

A. Yes.